

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:WR:NCA:SF:TL-N-612-98
JPThurston

date: JUN 01 1999

to: Assistant Chief Counsel (Field Service) CC:DOM:FS

from: District Counsel, Northern California District, San Francisco

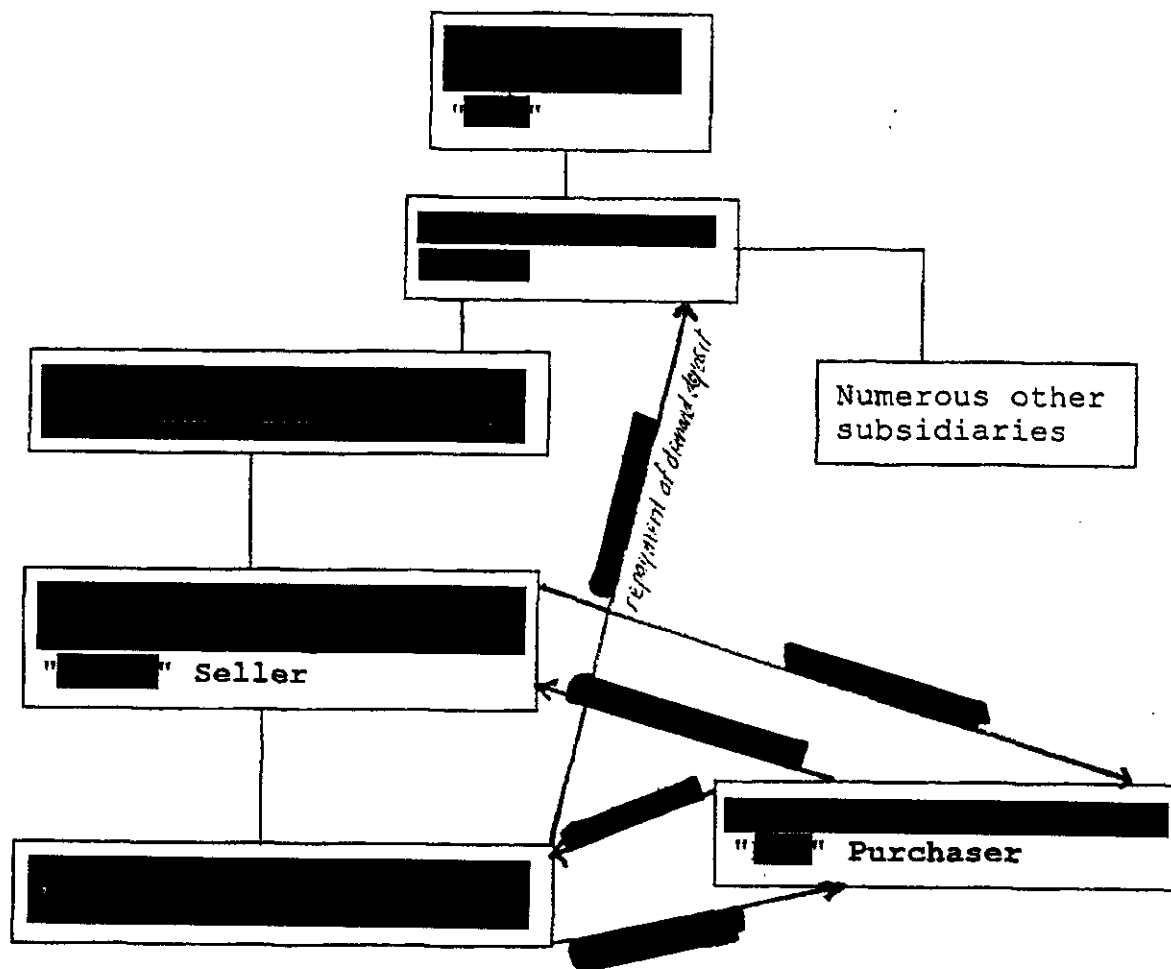
subject: Request for Post-Review of Significant Advice
Review of [REDACTED]

We request post-review of oral advice we offered the [REDACTED] audit team. The audit team requested our advice on the tax consequences of a sale of an [REDACTED] subsidiary to a third party purchaser.

We believe this advice qualifies for post-review under CCDM (35)3(19)4(4) because the advice involves the application of well-settled principles of law to the facts.

We have attached a copy of a Notice of Proposed Adjustment ("NPA") prepared by the [REDACTED] audit team setting forth facts and copies of relevant documents along with a proposed adjustment. We have been advised by the [REDACTED] audit team the NPA will not be issued to the taxpayer based in part upon the advice we offered.

Following is a diagram of the facts as set forth in the NPA:



On [REDACTED], [REDACTED] sold [REDACTED] to [REDACTED] for [REDACTED] Dollars (" [REDACTED] "). [REDACTED] The sale resulted in a capital loss claimed on the [REDACTED] consolidated income tax return of [REDACTED] in the amount of \$ [REDACTED]. The transaction was structured in two steps. First, [REDACTED] subscribed to stock in [REDACTED] in the amount of [REDACTED]. [REDACTED] used the capital to extinguish its sole liability, a [REDACTED] demand deposit from [REDACTED]. Second, [REDACTED] purchased for [REDACTED] all of the remaining stock of [REDACTED].

The [redacted] proposed to characterize the [redacted] equity subscription by [redacted] as part of the purchase price received by [redacted] for the stock of [redacted]. The [redacted] asserted that the value of the assets acquired by [redacted] was consistent with a purchase price of [redacted] instead of the [redacted] reflected in the sales agreement. The [redacted] states that the [redacted] demand deposit of [redacted] should have been included in the asset pool of [redacted].

We orally advised the audit team that the NPA position fails to take into consideration that the [REDACTED] was at all times both an asset and a liability. It was a liability payable to [REDACTED] before the demand deposit was paid off and it was a liability payable to [REDACTED], as a shareholder, after it was paid off. At no time did [REDACTED] have a net book value of [REDACTED] as asserted in the [REDACTED]. In fact, the net book value of [REDACTED] at closing was [REDACTED].

Moreover, to adopt the position taken in the [REDACTED] it would be necessary to attribute receipt of the [REDACTED] paid to [REDACTED] in satisfaction of the demand note as in substance received by [REDACTED] as part of the purchase price. The note payable to [REDACTED] would need to be disregarded. However, the \$[REDACTED] appears to be legitimate debt of [REDACTED] payable to [REDACTED] and no evidence is cited to the contrary.

The [REDACTED] could be considered part of the purchase price if [REDACTED] had been liable to [REDACTED] for the demand deposit. But there is no evidence that this was the case.

We advised that we did not think that the [REDACTED] equity subscription by [REDACTED] followed by the satisfaction of [REDACTED]'s [REDACTED] in indebtedness to [REDACTED] should be recharacterized as a payment of part of the purchase price by [REDACTED] to [REDACTED] for its [REDACTED] stock.

Please call Jim Thurston at (415) 744-9201 if you have any questions.


JAMES P. THURSTON
Special Litigation Assistant

Attachment

cc: Assistant Regional Counsel (TL)
(without attachment)